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MONTANA LOTTERY

FINANCIAL STATEMENTS
(Unaudited)

June 30, 2006

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MONTANA LOTTERY

FINANCIAL STATEMENTS
(Unaudited)

June 30, 2006

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APPOINTIVE OFFICIALS

George Parisot, Lottery Director

John Tarr, Lottery Assistant Director for Security

LOTTERY COMMISSION		TERM EXPIRES
Tom Keegan	Helena	January 1, 2010
Beth O'Halloran	Missoula	January 1, 2010
Robert Crippen	Butte	January 1, 2007
Wilbur Rehmann	Helena	January 1, 2009
Craig Anderson	Glendive	January 1, 2009

According to Section 23-7-202(9), MCA, copies of this report must be distributed to the following:

Governor – Brian Schweitzer
Director of Dept. of Administration – Janet Kelly
Legislative Auditor - Scott Seacat
President of the Senate – Jon Tester
Speaker of the House – Gary Matthews

The law also states "the President of the Senate and the Speaker of the House will determine the report distribution to each member of the appropriate committee of each house of the legislature". The President of the Senate and the Speaker of the House have requested that this report be distributed to the following committees:

HOUSE – State Administration Committee

Larry Jent, Chair
Dee Brown, Vice Chair Majority
Veronica Small-Eastman, Vice Chair Minority
Joan Andersen
Mary Caferro
Sue Dickenson
Emelie Eaton
Robin Hamilton
Gordon Hendrick
Teresa Henry
Hal Jacobson
William Jones
Gary MacLaren
Bruce Malcolm
Alan Olson
Bernie Olson

HOUSE – Business & Labor Committee

Jim Keane, Chair
Kathleen Galvin-Halcro, Vice Chair Majority
Joe McKenney, Vice Chair Minority
Elsie Arntzen
Bob Bergren
Tim Dowell
Kevin Furey
Dave Gallik
Ralph Heinert
Llew Jones
Mike Jopek
Harry Klock
Scott Mendenhall
Mike Milburn
Don Roberts
Wayne Stahl
Dan Villa
Jonathan Windy Boy

SENATE – State Administration Committee

Carolyn Squires, Chair
Joe Balyeat
Vicki Cocchiarella
Mike Cooney
Jon Ellingson
Jeff Essmann
Steve Gallus
Rick Laible
Dave Lewis
Jim Shockley
Joe Tropila

SENATE – Business & Labor Committee

Vicki Cocchiarella, Chair
Joe Balyeat
Duane Grimes
Dave Lewis
Glenn Roush
Frank Smith
Carolyn Squires
Donald Steinbeisser
Bill Tash
Jon Tester
Joe Tropila

Montana Lottery

September 2006

Montana Lottery Commission:

The Lottery experienced the highest sales ever in fiscal year 2006 and subsequently, the transfer to the General Fund will be the largest amount in the past ten years. The fourth quarter transfer of $2,709,469 compares very favorably to $1,526,239 transferred for the same time period last year. Total transfer for the year will be $9,110,455 compared to $6,222,555 last year, a 46% increase and 114% of our total projected transfer for the year.

Scratch sales continued to be strong with an increase of 6.7% over last year. Powerball experienced three runs resulting in jackpots in excess of $200 million including a record $365 million in February; resulting in total sales for 2006 of $18,888,081 or an increase of 36.0% over last year. Compared to fiscal 2005, Montana Cash sales were up by 19.2%, Wild Card up by 5.0% and Hot Lotto down by 1.7%. Total Qwik Tix sales were down 14.9% but seem to have now leveled out. Overall, sales were up 23.3% over last year.

Direct game costs were consistent with sales for the quarter and the fiscal year. Net operating revenue as a percent of total revenue is 36.7% for the quarter and 32.4% for the year to date. Total operating expenses of $779,137 for the quarter and $4,009,362 year to date are lower than last year's by 7.2%, though slightly higher than budgeted by 3.1%

In July and August, the Lottery returned to attending events around the state. The largest two were the Great Falls and Billings Fairs, where we participated for the full duration of the fairs. At the Billings location, we introduced the Family of Games as available only through that venue; however, we are now placing this product with our retailers. All indicators are present for a successful start to 2007.

Sincerely,

George Parisot
Director

2525 North Montana Avenue • Helena, MT 59601-0598
Phone 406-444-LUCK (5825) • Fax 406-444-5830

MONTANA LOTTERY
STATEMENT OF NET ASSETS
JUNE 30, 2006 and 2005
(UNAUDITED)

	Period Ended June 30, 2006	Period Ended June 30, 2005
ASSETS:		
CURRENT ASSETS		
Cash and Cash Equivalents	$ 2,365,054	$ 349,048
Receivables (Net)	904,280	1,349,901
Due from Primary Government	0	9
Due from Component Units	376	321
Inventories	1,394,354	1,100,853
Cash Collateral - Security Lending	33,830	
Other Current Assets	26,502	21,710
TOTAL CURRENT ASSETS	4,724,396	2,821,842
NONCURRENT ASSETS		
Computer, Furniture & Equipment	411,670	5,563,895
Accumulated Depreciation	(286,062)	(4,819,838)
Software, net of Amortization	0	123,214
Multi-State Receivable	1,394,278	1,326,136
TOTAL NONCURRENT ASSETS	1,519,886	2,193,407
TOTAL ASSETS	$ 6,244,282	$ 5,015,249
LIABILITIES:		
CURRENT LIABILITIES		
Accounts Payable	$ 298,500	$ 525,788
Estimated Prize Liability	1,565,400	1,436,459
Due to Primary Government	6,602	7,918
Due to Component Units	0	5
Transfer Obligations	2,709,470	1,526,239
Liability under Security Lending	33,830	
Deferred Revenue	203,786	100,634
Current Portion Comp. Absences	105,151	97,302
Current Portion Long-Term Debt	0	0
Other Current Liabilities	0	0
TOTAL CURRENT LIABILITIES	4,922,739	3,694,345
NONCURRENT LIABILITIES		
MUSL Prize Liability	1,241,969	1,257,803
Accrued Compensated Absences	79,574	63,101
TOTAL NONCURRENT LIABILITIES	1,321,543	1,320,904
TOTAL LIABILITIES	6,244,282	5,015,249
NET ASSETS		
Unrestricted Net Assets	0	0
TOTAL LIABILITIES AND NET ASSETS	$ 6,244,282	$ 5,015,249

The accompanying notes are an integral part of these financial statements.

MONTANA LOTTERY
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS
FOR THE QUARTERS AND YEARS ENDED JUNE 30, 2006 and 2005
(Unaudited)

	Quarter Ended June 30, 2006	Quarter Ended June 30, 2005	Year Ended June 30, 2006	Year Ended June 30, 2005
OPERATING REVENUES:				
Scratch ticket revenue	$ 2,570,368	$ 2,724,628	$ 11,239,757	$ 10,535,046
Powerball revenue	4,222,829	3,771,358	18,888,081	13,886,091
Montana Cash revenue	1,057,087	1,129,676	4,183,258	3,830,187
Wild Card revenue	661,374	610,603	2,416,577	2,301,163
Hot Lotto/Rolldown revenue	660,705	801,968	2,774,334	2,820,996
Qwik Tix revenue	140,105	95,678	416,407	437,762
License, permits, and misc	8,633	24,273	10,498	30,023
Total Operating Revenues	9,321,101	9,158,184	39,928,912	33,841,268
Less Direct Game Costs:				
Scratch ticket prize expense	(1,405,685)	(1,571,443)	(6,656,048)	(6,275,935)
On-line ticket prize expense	(3,284,520)	(3,239,469)	(14,071,484)	(11,527,966)
Retailer commission	(519,934)	(534,049)	(2,328,531)	(1,965,321)
Cost of tickets sold	(172,583)	(198,599)	(869,415)	(767,140)
Vendor fees	(521,311)	(754,828)	(3,083,535)	(2,822,415)
Net Operating Revenue	3,417,068	2,859,796	12,919,899	10,482,491
OPERATING EXPENSES:				
Advertising	95,272	301,078	493,318	606,394
Advertising Production	46,108	18,564	229,616	145,435
Audit Fees	9,881	3,577	71,483	22,333
Bad Debts Expense	(127)	20	(172)	3,187
Communications	22,362	23,769	87,880	91,550
Contractual Services	21,616	126,357	112,391	266,639
Depreciation and Amortization	7,201	267,640	790,777	1,069,531
Administrative Service Fee	13,485	13,579	53,942	54,318
State Cost Recovery	803	3,317	3,215	13,270
Multi-State Dues	0	0	72,333	88,856
Public Relations	24,123	18,143	37,110	27,318
Other	9,104	16,250	35,219	35,814
Personal Services	392,418	369,300	1,619,433	1,455,722
Repairs and Maintenance	2,326	9,594	11,100	24,822
Supplies and Materials	99,692	151,111	240,410	273,592
Travel	7,353	11,514	37,971	31,778
Utilities and Rent	27,520	28,208	113,336	111,067
Total Operating Expense	779,137	1,362,021	4,009,362	4,321,626
Operating Income	2,637,931	1,497,775	8,910,537	6,160,865
NONOPERATING REVENUES (EXPENSES)				
Interest earnings	71,531	27,082	199,910	62,033
Security Lending Income	1,985		1,985	
Security Lending Expense	(1,977)		(1,977)	
Gain/Loss on sale of asset	0	1,382	0	(343)
Total Nonoperating Revenues(Expenses	71,539	28,464	199,918	61,690
Income Before Operating Transfers	2,709,470	1,526,239	9,110,455	6,222,555
Operating Transfers In (Out) - General F	(2,709,470)	(1,526,239)	(9,110,455)	(6,222,555)
Total Operating Transfers Out	(2,709,470)	(1,526,239)	(9,110,455)	(6,222,555)
CHANGE IN NET ASSETS	0	0	0	0
Total Net Assets, Beginning of Period	0	0	0	0
TOTAL NET ASSETS, END OF PERIOD	0	$ 0	$ 0	$ 0

The accompanying notes are an integral part of these financial statements.

MONTANA LOTTERY
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN NET FUND ASSETS
AND RECONCILIATION OF BUDGET AND ACTUAL (BUDGETARY BASIS) TO GAAP BASIS
FOR THE TWELVE MONTHS ENDED JUNE 30, 2006
(Unaudited)

	Budget Fiscal Year July 1, 2005 - June 30, 2006	Actual Twelve Months Ended June 30, 2006 (Unaudited)	Actual as a Percent of Final Budget (%)
REVENUES:			
Scratch ticket revenue	$ $10,500,000	$ 11,239,757	107.05
Powerball revenue	17,500,000	18,888,081	107.93
Montana Cash revenue	4,400,000	4,183,258	95.07
Wild Card revenue	2,300,000	2,416,577	105.07
Hot Lotto revenue	2,650,000	2,774,334	104.69
Qwik Tix revenue	500,000	416,407	83.28
License, permits, and miscellaneous	2,000	10,498	524.90
Total Revenues	37,852,000	39,928,912	105.49
DIRECT GAME COSTS:			
Prizes - Scratch ticket	6,195,000	6,656,048	107.44
Prizes - Lotto games	13,311,000	13,821,408	103.83
Prizes - Qwik Tix	300,000	250,076	83.36
Retailer commissions	2,222,500	2,328,531	104.77
Ticket cost - scratch games	735,000	869,415	118.29
Ticket cost - vendor fees	3,160,475	3,083,535	97.57
Total Direct Game Costs	25,923,975	27,009,013	104.19
OPERATING EXPENSES:			
Advertising	633,390	493,318	77.89
Advertising Production	111,200	229,616	206.49
Audit Fees	45,000	71,483	158.85
Communications	69,790	87,880	125.92
Contractual Services	177,834	112,391	63.20
Administrative Service Fee	53,281	53,942	101.24
State Cost Recovery	3,143	3,215	102.29
Multi-State Dues	102,975	72,333	70.24
Public Relations	34,124	37,110	108.75
Other	31,220	35,219	112.81
Personal Services	1,513,170	1,643,755	108.63
Repairs and Maintenance	22,055	11,100	50.33
Supplies and Materials	203,688	240,410	118.03
Travel	35,186	37,971	107.92
Utilities and Rent	112,600	113,336	100.65
Equipment	45,839	49,115	107.15
Total Operating Expenses	3,194,495	3,292,194	103.06
Operating Income	8,733,530	9,627,705	110.24
NONOPERATING REVENUES (EXPENSES):			
Interest Earnings	0	113,870	
Security Lending Transactions		8	
Gain/(Loss) on Sale on Asset		0	
NET INCOME (BUDGETARY BASIS)	$ 8,733,530	$ 9,741,583	111.54
RECONCILIATION OF BUDGETARY/GAAP BASIS:			
1. Capitalized equipment purchases	45,839	49,115	107.15
2. Adjustment for compensated absences		24,322	
3. Adjustment for depreciation expense	(790,441)	(790,777)	100.04
4. Bad Debts		172	
5. MUSL interest earnings	20,000	86,040	430.20
Total Reconciling Items	(724,602)	(631,128)	
NET INCOME (GAAP BASIS)	$ 8,008,928	$ 9,110,455	113.75

The accompanying notes are an integral part of these financial statements.

ANALYSIS OF REVENUES AND EXPENSES BY PRODUCT
FOR THE YEAR ENDED JUNE 30, 2006
(UNAUDITED)

	SCRATCH	POWERBALL	MONTANA CASH	WILD CARD	HOT LOTTO	QWIK TIX	ADMIN
REVENUES:	$ 11,239,757	$ 18,888,081	$ 4,183,258	$ 2,416,577	$ 2,774,334	$ 416,407	$ 10,498
DIRECT GAME COSTS:							
Prize Expense	6,656,048	9,076,691	2,132,504	1,276,889	1,335,324	250,076	0
Retailer Commissions	893,861	944,916	209,218	120,869	138,758	20,909	0
Cost of Tickets Sold	869,415	0	0	0	0	0	0
Vendor Fees	859,304	1,470,297	322,698	185,126	215,026	31,083	0
NET OPERATING REVENUE	1,961,129	7,396,177	1,518,838	833,693	1,085,226	114,339	10,498
OPERATING EXPENSES:							
Advertising	124,397	249,326	38,202	38,202	37,005	1,744	4,442
Advertising Production	37,115	171,498	7,460	7,459	6,084	0	0
Audit Fees	0	0	0	0	0	0	71,483
Bad Debts	0	0	0	0	0	0	(172)
Communications	48,593	620	620	620	620	620	36,188
Contractual Services	1,813	9,190	498	498	498	755	99,139
Depreciation and Amortization	225,429	366,004	82,047	47,486	54,345	8,953	6,513
Administrative Service Fee	12,741	5,685	4,876	3,344	3,317	2,832	21,147
State Cost Recovery	0	0	0	0	0	0	3,215
Multi-State Dues	0	4,340	0	12,562	4,312	0	51,119
Public Relations	4,516	5,876	5,876	5,876	5,876	5,876	3,215
Other	1,720	2	2	2	3	21	33,468
Personal Services	549,019	180,578	141,369	86,270	85,249	73,570	503,378
Repairs and Maintenance	13	0	0	0	0	0	11,087
Supplies and Materials	70,101	4,327	4,442	4,274	4,274	3,359	149,633
Travel	1,050	302	302	302	302	0	35,714
Utilities and Rent	0	0	0	0	0	0	113,336
TOTAL OPERATING EXPENSES	1,076,507	997,748	285,694	206,895	201,885	97,730	1,142,905
OPERATING INCOME	884,622	6,398,429	1,233,144	626,798	883,341	16,609	(1,132,407)
NONOPERATING REVENUES (EXPENSES)							
Security Lending Transactions	0	0	0	0	0	0	8
Interest Earnings	0	0	0	0	0	0	199,910
TOTAL NONOPERATING REVENUES ENSES)	0	0	0	0	0	0	199,918
NET INCOME BY P	$ 884,622	$ 6,398,429	$ 1,233,144	$ 626,798	$ 883,341	16,609	$ (932,489)
PROFIT AS A % OF REVENUE	7.87%	33.88%	29.48%	25.94%	31.84%	3.99%	N/A

NOTE: THIS IS ONLY ONE YEAR'S ACTIVITY AND THEREFORE SHOULD NOT BE INTERPRETED TO SHOW HOW OUR PRODUCTS HAVE PERFORMED IN PAST YEARS OR WILL PERFORM IN THE FUTURE.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity.

The Montana Lottery, established under the provisions of Section 23-7-101, Montana Code Annotated (MCA), was approved by the Montana electorate through Legislative Referendum No. 100 on November 4, 1986.

Montana's first lottery tickets went on sale June 24, 1987.

The Montana Lottery is operated by a five-member commission consisting of Montana residents appointed by the Governor. The Commission, by law, has the power to operate a state lottery, determine the types and forms of lottery games, set the ticket price, number and size of prizes, conduct lottery drawings, enter into agreements to offer lottery games in conjunction with other lottery states and countries, and prepare financial reports. The Montana Lottery is attached to the Montana Department of Administration for administrative purposes.

The Montana Lottery is included as an enterprise fund in the State of Montana's Comprehensive Annual Financial Report. In accordance with governmental accounting and financial reporting standards, there are no component units to be included within the Montana Lottery's financial statements as a reporting agency.

Basis of Presentation. The Montana Lottery reports its financial activity in accordance with generally accepted accounting principles (GAAP) as prescribed in pronouncements of the Governmental Accounting Standards Board (GASB).

Enterprise Fund. The Montana Lottery is classified as an Enterprise Fund of the Governmental Proprietary Fund Type. Enterprise Funds account for operations: a) financed and operated similar to private business enterprises, where the intent of the Legislature is that costs are to be financed or recovered primarily through user charges, or b) where the Legislature has decided that periodic determination of revenue earned, expenses incurred, or net income is appropriate.

Basis of Accounting. The Montana Lottery's financial statements are prepared using the accrual basis of accounting. Revenues are recognized in the accounting period in which they are earned and become measurable; expenses are recognized in the period incurred, if measurable.

Revenue Recognition. Lottery scratch ticket sales are recorded as revenue based on the time the retailer activates the pack of tickets for sale. In accordance with an established policy, retailers may return unsold tickets to the Lottery for credit. Sales are decreased by an allowance for estimated ticket returns.

Ticket sales for lotto games, Powerball, Wild Card, Montana Cash, and Hot Lotto are recorded as revenue based on drawings. Tickets sold in advance for future drawings are recorded as deferred revenue until such time as the tickets become valid for the most current drawing. Qwik Tix revenue is recognized at the time of sale by the retailers.

Promotional Credits. The Lottery issues promotional credits to retailers to be used to distribute free tickets to players. The tickets are distributed as part of a promotion run by the retailer, e.g., "Ask for the Sale" or second chance drawings. The Lottery also directly distributes scratch tickets for promotional purposes at trade shows, for media give-aways, and during new game introductions. The tickets distributed as a result of promotional credits are reflected as a reduction in revenue. The related prize expense and ticket cost for all promotions are reclassified as an advertising expense. For the quarter ended June 30, 2006, promotional credits resulted in a revenue reduction of approximately $15,432 and an advertising expense reclassification of approximately $11,637. For the fiscal year ended June 30, 2006, promotional credits resulted in a revenue reduction of approximately $81,651 and a prize expense reclassification of approximately $64,045.

Prizes. Expenses for scratch prizes are recorded based on the predetermined prize structure for each game. Expenses for lotto and Qwik Tix prizes are recorded based on the predetermined prize structure for each individual game. No prize expense is recorded for free tickets distributed.

Unclaimed Prizes. Prizes for the lotto games must be claimed within six months after the appropriate draw date. Prizes for scratch games must be claimed within six months of the announced end of each game. Qwik Tix prizes must be claimed within six months of the sale date. The unclaimed prize amounts are taken as a reduction in the Lottery Prizes Payable liability and the Prize Expense and are transferred to the State of Montana General Fund as a portion of the quarterly transfer. The amount of unclaimed prizes for all games is represented in the table below.

	Quarter Ended 6/30/06	Quarter Ended 6/30/05	Year To Date 6/30/06	Year To Date 6/30/05
Lotto & Qwik Tix	$188,340	$140,996	$614,524	$534,630
Scratch	196,168	128,462	343,447	251,551
TOTALS	$384,508	$269,458	$957,971	$786,181

2. SUMMARY OF ACCOUNTS

Cash and Cash Equivalents. Cash and cash equivalents consist of interest-bearing deposits with the Montana Board of Investments short-term investment pool, cash on deposit with a bank and cash on deposit with the Montana State Treasurer that is part of the State's pooled cash and is not separately identifiable as to specific types of securities. These funds are highly liquid and may be drawn on daily.

Cash and cash equivalents consist of the following:

	June 30,	
	2006	2005
Short-term investment pool	$2,062,806	$186,928
Cash on deposit with State Treasurer	292,098	151,970
Cash in revolving deposit account	10,000	10,000
Petty Cash	150	150
TOTALS	$2,365,054	$349,048

Reference to the State of Montana's Comprehensive Annual Financial Report would identify the level of risk associated with cash and cash equivalents in the short-term investment pool and amounts retained with the State Treasurer. The bank balance of the revolving deposit account was $19,221 at June 30, 2006 and was covered by federal depository insurance. The carrying amount reported in the balance sheet for cash and cash equivalents approximates the fair market value.

Receivables. Receivables include $1,009,794, representing amounts due the Lottery for tickets purchased by retailers. An allowance for doubtful accounts is reported as net of receivables and is based on historical perspective. As of June 30, 2006 the allowance is zero. An allowance for ticket returns is also included in the receivables amount. This allowance represents a reduction in receivables at June 30, 2006, for estimated ticket returns. This is an estimate based on returns received to date, as well as, an estimate of tickets unsold by retailers for games that have a public sale end date prior to July 1, 2006. The allowance for ticket returns is $128,403 at June 30, 2006. The return of vendor fees related to the allowance for returns is $22,889.

Inventories. Inventories consist of merchandise and supplies inventories. Merchandise inventory includes scratch tickets valued at $1,295,163 stored in the warehouse, at retailers prior to being activated by the retailer and with the marketing representatives. These ticket inventories are recorded at cost using the specific identification method and maintained on a perpetual inventory system. Tickets are charged to cost of tickets sold upon activation or after game end.

Supplies inventories include ticket dispensers, premiums and point-of-sale materials. At quarter end, supplies inventories totaled $99,191. These inventories are also recorded at cost using the specific identification method.

Other Current Assets. Other current assets consist of the following:

	June 30,	
	2006	2005
Prepaid Expenses	25,034	19,960
Employee Advances	1,468	1,750
TOTALS	$26,502	$21,710

Transfer Obligations. The account "Transfer Obligations" is $2,709,470 payable to the General Fund at June 30, 2006.

Compensated Absences. State employees earn vacation leave ranging from 15 to 24 days per year depending on the individual's years of service. Vacation leave may be accumulated not to exceed two times the maximum number of days earned annually. With no limit on accumulation, sick leave is earned at 12 days per year. Upon retirement or termination, an employee is paid 100% for unused vacation and 25% for unused sick leave. The Lottery's liability for compensated absences is detailed below.

Balance June 30, 2005	Net Leave Earned/(Used)	Balance June 30, 2006
$160,403	$24,322	$184,725

Commissions. Section 23-7-301(10), MCA, provides retailers a commission on scratch, Qwik Tix and lotto tickets or chances sold. The Lottery Commission established this commission at 5% of the face value of scratch tickets activated by the retailers and the face value of Qwik Tix and lotto tickets sold. In addition retailers can earn bonus commissions on tickets sold based on incremental sales of scratch tickets. For the quarter and fiscal year ended June 30, 2006 retailers earned bonus commissions of $53,817 and $328,596 respectively. For the quarter and fiscal year ended June 30, 2006 total commissions were $519,934 and $2,328,531 respectively.

3. MARKETING PRODUCTION EXPENSES

The Lottery has contracted with several vendors to provide marketing related services and materials. These services include media placement, creative design and layout, and media production. Those services and materials not included in the Advertising and Advertising Production expense categories are printing and ticket dispensers. The cost of these services and materials, included in Operating Expenses as Contracted Services and Supplies and Materials, are detailed below for the fiscal year ended June 30, 2006:

Printing	$24,493
Ticket Dispensers	61,202
	$85,695

4. PAYMENTS TO OTHER STATE AGENCIES

The Lottery receives a variety of services and supplies and materials from other state agencies. These services and materials are detailed below for the fiscal year ended June 30, 2006:

Insurance	$ 18,212
Warrant Writing Services	1,075
Payroll Services	1,051
Audit Fees	48,030
Computer Fees	27,123
Printing	2,717
State Accounting System Support	11,140
Supplies and Materials	7,116
Mail Processing Fees	6,787
Telecommunications	17,550
Vehicle Rental Fees	1,017
Public Relations	7,000
Administrative Service Fees	53,942
SWCAP and SFCAP	3,215
Other	5,614
TOTAL	$211,589

5. PRIZES

Paid Prizes. Section 23-7-402, MCA states, "A minimum of 45% of the money paid for tickets or chances must be paid as prize money". Prize expense is recorded based on the predetermined prize structure percentage for each game less unclaimed prizes. For the quarter ended June 30, 2006, the prize expense of

$4,690,205 is 50.36% of net Lottery ticket revenue of $9,312,468. For the fiscal year ended June 30, 2006, the prize expense of $20,727,532 is 51.92% of net Lottery ticket revenue of $39,918,414.

6. TRANSFER TO STATE GENERAL FUND

Section 23-7-402(3), MCA, states "That part of all gross revenue not used for payment of prizes, commissions, and operating expenses, together with the interest earned on the gross revenue while the gross revenue is in the enterprise fund, is net revenue. Net revenue must be transferred quarterly from the enterprise fund established by 23-7-401 to the State General Fund." For the quarter ended June 30, 2006, the net revenue payable to the State General Fund totaled $2,709,470.

7. MULTI-STATE LOTTERY JOINT VENTURE

In November 1989 the Montana State Lottery joined the Multi-State Lottery Association (MUSL). MUSL was created in September 1987 to operate a multi-state lottery game for the benefit of party lotteries. Powerball, Wild Card, and Hot Lotto are the games jointly operated by the members, in which Montana presently participates. Each lottery participating in MUSL is represented on the Board of Directors.

The Multi-State Lottery Receivable with a balance of $1,394,278 as of June 30, 2006 is comprised of several reserve accounts, which are maintained by the Multi-State Lottery Association (MUSL). The balance of these reserve accounts is as follows:

Powerball Prize Reserve Account	$569,500
Powerball Unreserved Account	152,309
Powerball Set Prize Reserve Account	167,500
Wild Card Reserve Account	415,074
Hot Lotto Set Prize Reserve Account	89,895
TOTAL	$1,394,278

The Powerball Prize Reserve Account is to be used only in the event of an unanticipated prize claim. It is an insurance fund intended to protect the member lotteries against the liability that could result from a system failure at one of the member lotteries. All money paid to this fund would be returned to the Lottery one year after the Lottery leaves the Powerball game, assuming that no unanticipated prize claims have been paid. Interest earned on the Lottery's share of the fund, represented by the Unreserved Account, would be returned to the Lottery upon leaving MUSL. The amounts in the Unreserved Account may be used at the Board's discretion.

The Powerball Set Prize Reserve Account is used to fund prize payments for current drawings. Since the Powerball game has fixed prizes, it is often necessary to draw from this reserve to fund payment of prizes at the fixed amount. This account would be returned to the Lottery upon withdrawal from the Powerball Game.

The Lottery contributes to these reserve funds through the 50% set aside for prizes. In addition the Lottery was required to contribute for its portion of the reserve funds accumulated since the start of the Powerball game. The Lottery made this payment in full as of June 1990, through an additional 2% of drawing revenue rather than making a lump sum payment. Payments made to this fund are considered a portion of prize expense associated with the game.

The Wild Card Reserve Account is to be used in the event of an unanticipated prize claim on the Wild Card game. This account is also administered by MUSL and would be returned to the Lottery one year after the Wild Card Product Group of Idaho, Montana, South Dakota, and North Dakota is disbanded. The Lottery contributes to this account through the 55% set aside for prizes. Payments made to this fund are considered a portion of prize expense related to the Wild Card game.

The Hot Lotto Set Prize Reserve Account is administered by MUSL and is to be used only in the event of unanticipated prize claims. Like other MUSL games the reserve amount would be returned to the Lottery one year after withdrawal from the Hot Lotto game. The Lottery contributes to the reserve through the 50% set aside for prizes. Payments made to the reserve are considered a portion of the prize expense related to the game.

8. GAMES

Currently, the Montana Lottery games are scratch ticket games, four lotto games referred to as Powerball, Montana Ca$h, Wild Card, and Hot Lotto and four instant play/instant win games referred to as Qwik Tix.

Scratch ticket games provide players the opportunity to win instantly by scratching a latex covering to reveal a prize.

The Powerball game allows players the chance to win a minimum pari-mutuel jackpot of approximately $15 million. A player must match all 6 numbers to win the jackpot; players win prizes ranging from $3 to $200,000 for matching less than all 6 numbers. Drawings are held twice weekly on Wednesday and Saturday nights. For any drawing, if no ticket matches 6 out of 6 numbers, the jackpot rolls over to the next drawing to create a progressive jackpot. In March 2001, the Lottery added Power Play to the Powerball game. For an additional bet, the Power Play option provides non-jackpot winners the chance to multiply their prize amount by a factor of two through five.

The Montana Ca$h game allows players the chance to win a minimum pari-mutuel jackpot of $20,000. Players select 5 numbers from a field of 37 and must match at least 3 out of 5 to win a prize. Matching 3 of 5 wins $5 and 4 of 5 wins $200. The drawing is conducted twice weekly on Wednesday and Saturday nights. If no ticket matches all 5 numbers, the jackpot rolls over to the next drawing to create a progressive jackpot.

The Wild Card game allows players the chance to win a pari-mutuel jackpot, with a guaranteed minimum of $100,000. Players select 5 numbers from a field of 31 plus one of 16 face cards and must match all 5 numbers and the wild card to win the jackpot; players win prizes from $1 to $5,000 for matching less than all 5 numbers and/or the wild card. Drawings are held twice weekly on Wednesday and Saturday nights. If no ticket matches all 5 numbers and the wild card, the jackpot rolls over to the next drawing to create a progressive jackpot.

Hot Lotto allows players the chance to win a pari-mutuel jackpot with a guaranteed minimum of $1 million. Players choose 5 numbers from a field of 39 plus 1 Hot Ball number from a field of 19; the first 5 numbers and the Hot Ball must be matched to win the jackpot. Players can win prizes ranging from $2 to $10,000 by matching less than all 5 numbers and/or the Hot Ball. If no ticket wins the jackpot, it rolls over to the next drawing to create a progressive jackpot. Drawings are held twice weekly on Wednesday and Saturday nights.

Qwik Tix is a product line introduced by the Lottery in February 2004. There are four games, each with its own play style and prize structure. The four games are Lucky Numbers, a number match game; Hot Tac Toe, a tic tac toe grid; Jacks or Better, a poker game; and Montana Match, a match three symbols game. The Qwik Tix tickets are printed at the lotto terminal at the time of sale and can be redeemed immediately, with the maximum prize being $500. Each ticket costs $2 and consists of two plays of a single Qwik Tix game.

9. COMMITMENTS - GAMING SUPPLIER CONTRACTS

Scratch Tickets. On June 27, 2001 the Montana Lottery Commission approved the award of a one-year contract with Oberthur Gaming Technologies Corp. (Oberthur) for the provision of scratch tickets; the resulting contract was signed on August 8, 2001. The contract is for one year with the option for six additional one-year renewals. The contract contains specifications regarding ticket design, printing, game ownership, inspection, and prize structure.

Oberthur, as the vendor, provided a performance bond covering the contract term and an errors and omissions policy covering an ultimate net loss of $7,500,000. The Lottery may terminate this contract by providing proper notification to Oberthur.

On-line Services. On August 18, 1998, the Lottery signed a seven-year contract with Autotote Lottery Corporation to provide an on-line gaming system and associated services beginning March 28, 1999. The contract provides for payments to be made for the purchase of an on-line gaming system including terminals and software. The Lottery paid Autotote Lottery Corporation $5,025,311 for the system on April 26, 1999. Payment under the contract is also based on 8.35% of weekly Lottery sales. This contract expires on March 30, 2006.

On October 11, 2005, the Lottery signed a seven-year contract with Intralot, Inc. of Duluth, GA to provide an on-line gaming system and the associated services beginning March 31, 2006. The contract requires Intralot to provide new terminals to all retailers with the associated software and communications. Payment under the contract is based on 5.8% of net weekly Lottery sales. The contract provides for three one-year extensions, if agreeable by both parties.

10. CONTINGENT LIABILITIES - PRIZE ANNUITIES

During fiscal year 1989, the Montana Lottery awarded four Big Spin Jackpot prizes totaling $5,000,000. The Lottery made the initial payments to the winners in the amount of $253,088 and on September 26, 1988 the Montana Lottery awarded annuities in the amount of $2,350,180 to Western National Life. Through these annuities, Western National Life makes the remaining payments to the Big Spin Jackpot winners. As of June 30, 2006 the contingent liability for future prize payments funded through the purchase of annuities was $232,500.

11. LOTTO*AMERICA/POWERBALL/TRI-WEST JACKPOT PRIZES

Jackpot prizes awarded in the Lotto*America/POWERBALL and TRI-WEST LOTTO games are funded through the purchase of U.S. Treasury Zero-Coupon Bonds purchased in the name of the Montana Lottery by MUSL. MUSL will cash the bonds each year as they mature and will wire the funds to the Lottery for payment to winners on the Anniversary date of the win.

On January 13, 1990 the Montana Lottery awarded its first Lotto*America jackpot prize totaling $1,740,000. The first annual payment of $87,000 was made on February 1, 1990. On May 9, 1990 the Lottery awarded a second Lotto*America jackpot prize of $3,000,000. The first annual payment of $150,000 was made on May 23, 1990. A third jackpot prize was awarded on February 2, 1991 for $7,360,000. The first annual payment of $368,000 was made February 15, 1991. On November 23, 1991 a fourth jackpot prize was awarded totaling $46,967,738.57. The first annual payment of $2,355,738.57 was made December 12, 1991. On April 11, 1992 a fifth jackpot prize was won totaling $2,000,000. The first annual payment of $100,000 was made on April 27, 1992.

On July 6, 1994 the Montana Lottery awarded its first Tri-West Lotto jackpot prize totaling $700,565. The first annual payment of $35,000 was made on July 26, 1994.

On July 22, 1995 the Montana Lottery awarded its first Powerball jackpot prize totaling $31,401,655.99. The first payment of $1,571,655.99 was made on August 8, 1995. On April 5, 1997 the Lottery awarded a second Powerball jackpot prize totaling $11,000,000. The first annual payment of $550,000 was awarded on April 18, 1997.

As of June 30, 2006 the combined total of future prize payments funded through the purchase of U.S. Treasury Zero-Coupon Bonds for Lotto*America winners was $14,423,739. The combined total of future prize payments funded through the purchase of U.S. Treasury Zero-Coupon Bonds for Powerball and Tri-West Lotto winners was $19,910,210.

On March 27, 1999 the Montana Lottery had a Powerball jackpot winner. The prize was $35.1 million ($19.35 million cash option). The winner chose the cash option and was paid a lump sum in June 1999.

12. LEASES

Rent. The Montana Lottery leases its office, administrative and warehouse facilities under a noncancelable lease agreement that is effective March 2002 through February 2007. The monthly lease payments through February 2007 are $7,588.

13. INVESTMENT RISK DISCLOSURES

Effective June 30, 2005, the State of Montana implemented the provisions of Governmental Accounting Standards Board (GASB) Statement No. 40, *Deposit and Investment Risk Disclosures*. The Lottery participates in two investment pools: the Multi-State Lottery Association (MUSL) reserve accounts and the State of Montana's Short Term Investment Pool (STIP). There are four types of risk that must be disclosed. These risks are defined below, followed by their applicability to each of the investment pools.

Credit risk is defined as the risk that an issuer of an investment will not fulfill its obligation, i.e., not make timely principal and interest payments.

Custodial credit risk is the risk that the Lottery would not be able to recover the value of the investment or collateral securities that are in the possession of an outside party in the event of the failure of that party.

Concentration of credit is the risk of loss attributed to the magnitude of a government's investment in a single issuer.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment.

Multi-State Lottery Association The MUSL investment policy for prize reserve and unreserved funds states that permitted investments "include direct obligations of the United States government, perfected repurchase agreements, and obligations issued or guaranteed as to payment of principal and interest by agencies or instrumentalities of the United States government, and mutual funds of approved investments". Obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government are not considered to have credit risk nor concentration of credit risk per GASB Statement No. 40.

The securities are held in trust for MUSL by Mellon Trust. This large diversified institution was chosen to minimize custodial risk. It has several national offices, with the Everett, Massachusetts office handling the MUSL account. Interest rate risk is minimized by requiring that the average portfolio maturity be no more than 1.33 years and that the maximum maturity for any one security cannot exceed five years.

Short-term Investment Pool All short-term funds are held in the State's Short Term Investment Pool (STIP) administered by the Board of Investments (BOI). A summarized description of their disclosure follows and full details may be obtained by contacting the Montana Board of Investments, 2401 Colonial Drive, PO Box 200126, Helena, MT 59620-0126.

For STIP securities, BOI's policy to manage credit risk requires securities have the highest investment grade rating in the short-term category by at least one Nationally Recognized Statistical Rating Organization (NRSRO). The six NRSROs include Standard and Poors, Moody's, Duff and Phelps, Fitch, IBCA and Thompson's Bank Watch.

Per the BOI, all STIP securities are registered in the nominee name for the Montana Board of Investments and held in the possession of the Board's custodial bank. The STIP investment policy does not specifically address concentration of credit risk. However, as of June 30, 2005 there were no single issuer investments that exceeded 5% of the STIP portfolio. Per GASB Statement No. 40, interest rate disclosures are not required for STIP since STIP is a 2a-7-like pool.

Alternative accessible formats of this document will be provided upon request.